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PROTECTIONISM AND STRUCTURAL ADJUSTMENT

Problems of protectionism and structural adjustment

Report by the UNCTAD secretariat

PART I: RESTRICTIONS TO TRADE

PART II: MAJOR STRUCTURAL DEVELOPMENTS IN THE WORLD ECONOMY AND EXPORT PROSPECTS OF DEVELOPING COUNTRIES

For a statistical and information annex containing supporting information for this report, see TD/B/1282/Add.1.

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SUMMARY AND POLICY ISSUES

(i) The slight deceleration in the growth of world trade since 1988 has reflected mainly somewhat slower expansion of output in developed economies, but also the important decline in the growth of output and imports in some of the more industrialized developing economies in South-East Asia and to continued stagnation in others. In many developing countries, supply side factors also contributed to the export slowdown. In the case of several countries in Eastern Europe, exports fell largely on account of supply problems. Thus a revitalization of growth in the developing world and the reconstruction of Eastern Europe would have very favourable effects on the evolution of world trade and world economic growth.

(ii) There has been considerable trade policy reform in the USSR, countries in Eastern Europe and in developing countries. The USSR and Eastern European countries are now fully committed to liberalizing their trade régimes and to integrating their economies in the international trading system. Developing countries in all regions have generally continued to liberalize their trade régimes. Trade policy reforms which in recent years have taken place in numerous Latin American countries have resulted in a reduction of tariffs, a simplification of tariff structures and a dismantling of most non-tariff measures, contrasting with previous policies in favour of import substitution.

(iii) Developed countries have taken steps to support the reform process in the USSR and in countries in Eastern Europe, *inter alia* by providing them with more favourable tariff status and by dismantling specific non-tariff measures. Trade liberalization measures in favour of developing countries have been modest. New trade distorting measures have been very few in number. However, most of the quantitative restrictions or measures having similar effects which existed before the launching of the Uruguay Round were still in force in December 1990. The share of trade covered by NTMs has not diminished to any significant extent.

(iv) In spite of sustained economic growth and consequently high level of capacity utilization, the stock of outstanding anti-dumping cases, particularly those involving developing countries, has continued to increase in recent years. The persistent use of anti-dumping actions and the widening of the scope of their application in some countries continues to cause concern that anti-dumping laws are being used for protectionist purposes.

(v) The GATT enabling clause allows developed countries to provide tariff preferences to developing countries with a view to supporting their industrialization and development process. A series of developments have eroded preferential tariff treatment for developing countries, particularly the new free trade agreements between developed countries; the granting of GSP status to some countries in Eastern Europe; and the exclusion of certain major developing country exporters of manufactured products from the GSP schemes of certain preference giving countries. Consequently in a number of cases, trade weighted average import duties applied on imports originating in developing countries are higher than on imports from other developed countries.

(vi) The effects of tariff concessions in the Uruguay Round negotiations on exports from sub-Saharan countries may be quite different for each of the major markets. Considering the tariff offers by major industrialized countries as at the end of July 1990, on an aggregate basis, the African region is the only one among the developing regions that experiences a net loss in export revenues, in both tropical products and natural resource-based products.

(vii) While the once-and-for-all increase in income which the formation of a single EEC market is expected to bring about may yield export gains to developing countries, the removal of internal barriers within the Community and its southward enlargement are, on the other hand, likely to lead to some displacement of their imports by supplies from within the Community. The net impact remains a matter for speculation. Protectionist pressures within the EEC need to be kept at bay, if the completion of the Single Market and the full incorporation of its new members are to have stronger trade creating than trade diverting effects.

(viii) As the East European economies become more open to international trade, developing countries may gain opportunities to increase their exports to the countries in Eastern Europe. Whether these opportunities will materialize or not will depend on the trade policies of these countries. A strong commitment to open markets would lead to the most beneficial effects on the exports of developing countries.

(ix) In the short term, countries in Eastern Europe are unlikely to generate competitive exports which are sufficiently large to replace exports from developing countries to developed countries on a substantial scale. Over the medium term, structural changes in countries in Eastern Europe could move export production to a greater extent into sectors in which developing countries have established export supply capabilities. Competititon could increase in some commodity and manufacturing sectors. Developed countries need to ensure that the preferential market access they grant to the countries in Eastern Europe does not have adverse effects on the exports of manufactures of developing countries.

(x) Industrial restructuring continues to be a central objective of Japan's economic policy. Steps have also been taken to ease access to the domestic market. As a result of these policy measures and of enterprise strategies to cope with the rise in the yen, imports of manufactures have increased strongly in recent years. Japan's imports of manufactures from developing countries remain, however, highly concentrated on suppliers in South-East Asia. The growth of Japanese imports should be further encouraged through both market opening measures and further adjustment to source abroad Japan's needs for labour-intensive manufactures. Developing countries which have not yet significantly benefitted from the Japanese import boom need to build competitive supply capabilities in products the demand for which is growing rapidly in the Japanese market.

(xi) The obdurate nature of the United States trade deficit could, in no small part, be the result of a decline in the competitiveness of the productive base of the United States relative to those of its major trading partners. The strengthening of competitiveness depends crucially on the initiation of a more vigorous process of structural adjustment, while defensive trade policies should be phased out.

(xii) Since the early 1980s, a growing number of developing countries have pursued policies aimed at increasing the openness of their economies. Their experience seems to show that a staged process of import liberalization, with due attention paid to building up supply capabilities, is likely to lead to more successful structural adjustment than a rapid and broad-based liberalization of imports. As the number of countries adopting trade liberalization and export promoting strategies grows, so does the need for developed countries to preserve open markets or improve market access conditions for the exports of developing countries. This would be facilitated by the adoption of positive structural adjustment measures and mechanisms.

(xiii) At the seventh session of UNCTAD, member States agreed that their commitments expressed in past resolutions to halt and reverse protectionism and those relating to structural adjustment should be fully implemented. They also agreed that there should be improvements in the access to markets, particularly for products of export interest to developing countries. The Trade and Development Board reaffirmed those commitments at the second part of its thirty-fifth and thirty-sixth sessions. In general, however, there has been no significant improvement in market access conditions for developing country exports, despite some progress towards liberalization on the part of some developed countries. Greater efforts aimed at promoting structural adjustment policies in developed countries were necessary if the protectionist policies were to be reversed to a significant extent. Developing countries, on the other hand, have pursued their trade liberalization policies seeking to improve the international competitiveness of their productive base and export supply potential. The second part of the thirty-seventh session of the Board provides a timely opportunity for addressing the main issues in this area, which should contribute to the consideration of the same issues at UNCTAD VIII.

PART ONE

RESTRICTIONS TO TRADE

Chapter I

RECENT TRENDS IN WORLD TRADE

1. Since August 1990, the outbreak of the Persian Gulf crisis has been the dominant event on the international economic scene, with potential adverse consequences for world economic growth and international trade. The crisis occurred against the background of a weakening world economy. Even before its outbreak, world trade had lost already some of its momentum. The 7 per cent rise in the volume of world trade in 1989 was well below the record 9 per cent achieved in 1988. Growth is estimated to have decelerated further in 1990, perhaps to the 5-6 per cent level.

2. Prominent features of the evolution in the volume of trade in 1989 were slightly slower growth of exports from developed market-economy countries (7 per cent as compared to 8 per cent), a significant deceleration in the growth of exports from developing countries (down to 6 per cent from 9.6 per cent in 1988) and a dismal export performance of countries in Eastern Europe, which recorded a decline in their exports (-1.6 per cent). The growth of China's exports slowed down, but remained strong (8 per cent). Apparently, these trends continued in 1990. Estimates indicate that export growth of the developed market economies and the developing economies slowed down further, and the decline in exports from Eastern Europe became more pronounced (see annex tables I.2 and I.5). In this latter geographical region, the decline in East-East trade has been even steeper than in trade with other regions.

3. The deceleration in the growth of world trade reflected mainly the slower output expansion in developed market economies, but also the important decline in the growth of output in the relatively more industrialized South-East Asian economies, leading to a lower demand for internationally traded goods. Moreover, slower growth for 1990 has been projected in the wake of the oil price increase. In developing countries, supply side factors also contributed to the export slowdown. In the case of several countries in Eastern Europe, exports fell largely on account of supply problems (see annex table I.4). In 1990, the accelerating contraction of East-East trade, in particular, reflected to a large extent the acute difficulties experienced by the Soviet Union in meeting commitments for oil delivery.

4. While the volume growth of exports from South and South-East Asia decelerated in line with the general trend, the region still recorded an expansion of exports at a significantly faster pace than Africa and Latin America. In the case of major exporters of manufactures (Hong Kong, the Republic of Korea, Singapore and Taiwan Province of China), the main causes of the export slowdown were rising wages, domestic inflation and, in particular, currency appreciation, reducing the international competitiveness of their manufactured exports. In contrast, continued strong growth of exports of several new exporters of manufactures in the region (Indonesia, Malaysia and Thailand) has, in no small part, been due to the competitive advantage which they enjoy because of relatively low wages and continued investment by Japanese firms to supply the Japanese market (see annex tables I.2 and I.3).

5. The growth of Latin American exports has decelerated considerably since 1988 (see annex table I.2). Although the region as a whole continues to be highly dependent on primary commodity exports, a growing number of countries have developed supply capabilities in manufactures. In several countries, among them Argentina and Brazil, domestic instability, the burden of debt and inadequate private investment have not allowed for a self-sustained expansion of exports

and output and have had strong adverse effects on the manufacturing sector. Some other countries, such as Chile, Colombia, Costa Rica, and Mexico, have recorded sizeable advances in exporting their manufactured products in the recent past. Chile diversified its export base considerably in the 1980s. The recent increase in exports has encompassed manufactures, copper and other agro-industrial products. In the case of Mexico, whose dependence on oil exports is much smaller now than some ten years ago, part of the expansion in manufactured exports has come from the re-orientation of existing capacity by United States corporations from the domestic market to supply markets in the United States.

6. For Africa, export earnings continue to be at the mercy of the vagaries of primary commodity prices. Manufactured exports to developed market-economy countries, essentially the EEC, continued to grow in value terms (see annex table I.3), but these exports originated in only a few African countries and, on the demand side, represented a very small percentage of total manufactured imports by the developed economies. Many countries in Africa are still dependent on only one or a small number of manufactured export products. Investment has remained low and poor transportation links with major overeas markets, in particular the United States and Japan, constrain export market diversification.

7. The resumption of economic growth in those developing countries which have not participated in the world economic expansion of the 1980s would have a beneficial impact on world trade. Most countries in Africa and Latin America (and many in Asia which are not major exporters of manufactures) have had to postpone import increases or even reduce their import levels, particularly of capital goods. Any spurt in investment and output growth is likely to lead to a more-than-proportional rise in import demand. The same can be said for the countries in Eastern Europe. Given the intention of the Governments of several of these countries to hasten the integration of their economies into international markets, the impact on world trade of success in the restructuring of these economies could be large. Policies which alleviate balance-of-payments stringencies (including debt relief and larger transfers of financial resources) and improve access to markets for the exports of these countries would contribute to faster economic growth and to an increase in import levels.

Chapter II

DEVELOPMENTS IN TRADE ACTIONS AND TRADE LEGISLATION IN 1990

8. The process of reform in the USSR and countries in Eastern Europe continued at a rapid pace. The USSR and Eastern European countries are now fully committed to liberalizing their trade régimes and to integrating their economies in the international trading system. Simultaneously, these countries obtained easier conditions of market access in Western Europe and in the United States.

9. Developing countries as a whole continued to liberalize their trade régimes, but a special feature in 1990 was the substantive changes in Latin American countries. Trade policy reforms which in recent years have taken place in numerous Latin American countries have resulted in a reduction of tariffs, a simplification of tariff structures and a dismantling of most non-tariff measures.

10. The United States abstained from naming any countries or practices under the "Super 301" Section of the Omnibus Trade and Competitiveness Act of 1988, which had been of great concern to trading partners since the 1989 announcements. However, 23 countries remained on the "watch lists" in the context of the provisions known as "Special 301".

11. A number of quantitative restrictions on imports from countries in Eastern Europe were eliminated, particularly in the EEC, with a view to supporting the efforts of these countries to strengthen their economic relations with the rest of the world. Some other quantitative restrictions

in OECD countries were eliminated during 1990, in a number of cases following panel reports under GATT's dispute settlement mechanism. However, most of the quantitative restrictions or measures having similar effects which existed before the launching of the Uruguay Round were still in force in December 1990.

12. The number of newly initiated anti-dumping and countervailing duty actions continued to fall compared to its peak level in the mid-1980s, probably in line with sustained economic growth. However, in most countries the stock of outstanding cases has not diminished to any significant extent. The persistent use of anti-dumping actions and the widening of the scope of their application in some countries in recent years continued to cause concern that anti-dumping laws are being used for protectionist purposes.

A. Salient actions taken in 1990

1. Trade actions in developed countries

13. The May 1990 announcements by the United States Trade Representative (USTR) did not target any countries under the provisions which require the identification of "priority trade practices", and of "priority countries".[1] The USTR had initiated six "Super 301" investigations involving Brazil, Japan and India, in 1989. However, it did not take any retaliatory actions. Consultations were held with Japan on forest products, supercomputers and satellites. Following the conclusion of bilateral agreements USTR formally suspended its investigations on 22 June.[2] The investigation against Brazil was terminated in May 1990, after the new Government removed quantitative import restrictions and prohibitions. India refused to enter into negotiations with the United States under the threat of retaliation. The USTR determined for the second year in a row that India's trade practices[3] were "unreasonable" under the Super 301 provision. However, the United States decided not to impose sanctions on the grounds that they would be inapropriate at this time, while negotiations on services and investment were under way in the Uruguay Round.

14. However, 23 countries remained on the "watch lists", in the context of provisions requiring USTR to identify foreign countries which deny adequate and effective protection to United States intellectual property rights.[4]

15. Few trade restraining measures were reported in 1990. Invoking GATT Article XIX, Austria introduced a quota for imports of certain prepared fowls, effective March 1990. National restrictions applied by member States of the EEC were in some cases superseded by voluntary export restraints at the Community level. VERs on footwear were concluded with the Republic of Korea and Taiwan, Province of China, in June 1990.[5] Following the expiration of the bilateral MFA agreement with Thailand on 31 December 1988, the United States imposed unilateral restrictions on imports of certain textile categories. A threat of a new trade conflict arose after the European Community announced a ban on imports of meat from the United States following a decision of the EC's Standing Veterinary Committee claiming that the United States did not meet EC's veterinary standards. Imports of all pork products were banned on 31 October 1990. Beef and all other fresh meat products, except sheep and horse meat, were banned on 30 November.

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1 This statute is known as "Super 301".

2 The investigations were suspended rather than terminated because under the Super 301 provisions, the cases must be left open until a three-year revision of the pact's success has been conducted.

3 The United States alleged that India' barriers to US investment and exclusion of US insurance companies were an unreasonable burden to US commerce.

4 These provisions are known as "Special 301". Brazil, India, China and Thailand remain on the "priority watch list". The 19 trading partners still on the "watch list" are: Argentina, Canada, Chile, Colombia, Egypt, Greece, Indonesia, Italy, Japan, the Republic of Korea, Malaysia, Pakistan, the Philippines, Saudi Arabia, Spain, Taiwan Province of China, Turkey, Venezuela and Yugoslavia. Mexico and Portugal were removed from the watch lists.

5 See: Regulation (EEC) 1735/90 of 21 June 1990, *Official Journal of the European Communities*, L 161 of 27 June 1990.

16. A number of quantitative restrictions were eliminated during 1990, most of them in favour of countries in Eastern Europe. A series of developments took place in the EEC, particularly with regard to national quantitative import restrictions applied by member States, under Regulation (EEC) 3420/83. In late 1989 specific quantitative restrictions on imports from Poland and Hungary were suspended. Quantitative restrictions on imports from the USSR and Czechoslavakia were significantly reduced in May and July 1990, respectively. In July 1990 all restrictions facing the former German Democratic Republic were suspended. Finally, in October, all specific restrictions on imports from Bulgaria, Czechoslovakia and Romania[6] were suspended until the end of 1991. A number of quantitative restrictions on imports from Yugoslavia were also suspended.[7]

17. Certain EC member States further eliminated quantitative restrictions, *inter alia* on imports originating in Japan, in November 1990.[8] Some remaining hard-core national measures will have to be dealt with in connexion with the completion of the single market at the end of 1992.[9]

18. Quantitative restrictions were lifted in some instances after having been challenged under the GATT dispute settlement mechanism. Following a GATT panel report finding that sugar import quotas were in violation of international trade rules, the United States replaced quotas by a tariff quota system, effective 1 October, 1990.[10] Japan continued to implement previously announced market opening measures.

19. Other trade liberalization measures were reported as follows: Australia and New Zealand established a free trade area as all trade beween the two countries was exempted from import duties, quantitative restrictions (such as VERs on trade in dairy products) and anti-dumping measures, effective 1 July 1990. The Australian Government removed import controls applying to second-hand material handling equipment effective from 10 December 1989. Access to the Japanese market was further improved as tariffs were suspended on 1004 manufactured products and reduced on four other manufactured products. Finland abolished part of the quantitative restrictions (quotas and licensing) on imports of agricultural products, effective June 1990. The EEC did not seek renewal of VERs concerning steel trade with Venezuela and the Republic of Korea. In June 1990, the United States lifted tariffs which had been imposed in October 1988 on certain products imported from Brazil, in retaliation of alleged lack of intellectual property protection for pharmaceuticals.[11]

20. In order to maintain the level of trade of the former German Democratic Republic with its trading partners in Eastern Europe and the USSR after the German unification, which would imply the immediate application of Community commercial policy, the European Communities adopted certain transitional measures in this regard. The measures, which would be applicable from December 1990 until the end of 1991 with the possibility of renewal for another year, included: establishment of tariff quotas, for maximum duty-free amounts equal to the quantities or values contained in the German Democratic Republic's bilateral agreements,[12] and suspension of certain quantitative restrictions.[13] The beneficiaries of these measures would be the USSR, Poland

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6 Suspension of restrictions to Romanian imports is pending the entry into force of a bilateral trade agreement with Romania.

7 As from 1 October 1990, restrictions facing Yugoslavia under Regulation (EEC) 288 82 were suspended until 31 December 1991, except for certain products imported into Spain or Portugal. (Council Regulation (EEC) 2727 90 of 25 September 1990).

8 Regulation (EEC) 3156 90 of 26 October 1990, published in OJ L 304 of 1 November 1990.

9 The EC Commission, in a report on the "Single Community Motor Vehicle Market" proposed to eliminate national restrictions currently applied against imports of Japanese cars in five member States (France, Italy, Portugal, Spain and the United Kingdom). However, Community producers would be allowed time for adjustment measures during a transitional period. Protection will likely be provided through a Community wide VER. Deliberations were going on, especially on the question whether or not to include cars produced within the Community as well as on the duration of the transitional measures. (See: EEC working paper SEC(89) No. 2118 of 18 January 1990).

10 Under the tariff quota system a quantity of sugar, subject to prevailing tariff rates, is allocated by the USTR on a country-by-country basis, on the basis of historical trade flows. The within quota rate was maintained at 0.625 cents per pound, while the above quota rate was set at 16 cents per pound. The quota amount for 1989 90 was set at 1,725,000 metric tons.

11 The retaliatory tariffs were lifted following a decision of the Brazilian Government to adopt legislation protecting pharmaceutical product and process patents.

12 Imports under these quotas would have to be for final consumption in the former GDR territory. The arrangements, according to the EEC, did not apply to agricultural products.

13 The major proportion of such restrictions previously applied to imports from European COMECON countries have

Hungary, Czechoslovakia, Romania, Bulgaria, and Yugoslavia.

21. The EEC and the members of EFTA formally started negotiations aiming at the creation of the European Economic Space (EES), which includes *inter alia* the free circulation of goods, services and capital. The EES may come into force on 1 January 1993, at the same time as the completion of the EEC internal market. The EC Commission received a mandate to negotiate a free-trade agreement with the countries of the Gulf Co-operation Council.

22. Under the "Enterprise for the Americas" initiative, the President of the United States proposed new economic ties with Latin America, covering trade, investment and debt, on 27 June, 1990. The United States proposed to negotiate framework agreements for discussing trade issues with groups of or individual countries in the region, which might result in establishment of Free Trade Agreements comparable to the agreement being negotiated with Mexico. Framework agreements, creating working groups to monitor trade and investment, open markets and negotiate future trade agreements were signed with Bolivia, Chile and Colombia. A similar agreement between the United States and Brazil, Argentina, Paraguay and Uruguay is being negotiated.

23. Actions by members of the Group of 24 aid donor countries resulted in improved tariff treatment for countries in Eastern Europe. The United States granted MFN status to Czechoslovakia.[14] Mutual steps were taken to extend such status to Bulgaria[15] and the USSR.[16] The Support for East European Democracy (SEED) Act of 1989 made Poland eligible for GSP tariff status (which it formally obtained on 5 January 1990). Hungary had received GSP status in November 1989. The EEC provided GSP tariff treatment to Hungary and Poland, since 1 January 1990. Starting the same date, Japan and Austria extended GSP benefits to Poland. The European Commission proposed to provide GSP status to Czechoslovakia and Bulgaria and to eliminate exclusions of a series of industrial products applied to Romania, effective 1 January 1991.

24. Both the EEC and the United States improved GSP benefits for the Andean countries. In November 1990, the EEC decided to extend, during four years, the GSP treatment granted to least developed countries to Bolivia, Colombia, Ecuador and Peru.[17] In the United States, GSP benefits for Andean countries were expanded as a result of the annual GSP review in combination with a special GSP review carried out for Bolivia, Colombia, Ecuador and Peru. The United Stated also expanded GSP benefits to Mexico and Brazil. Bahrain was re-designated as a GSP beneficiary.

2. Trade actions in developing countries

25. One of the salient developments in the last few years has been the far reaching process of trade liberalization in Latin America and in some of the Caribbean countries. Tariff structures have been simplified and rates have been reduced significantly. A number of countries[18] have bound their full tariff schedules in GATT (recent tariff policy measures are summarized in tables I.7a and I.7b). Non-tariff measures have been substantially reduced or even fully eliminated in the majority of countries (see table I.8). Consequently the incidence of NTMs in Latin American imports is now much smaller than that in developed country imports from Latin America. The liberalization process continued in 1990, especially in Brazil and Peru, where the newly elected Governments dismantled most of the existing quantitative restrictions. Brazil adopted a series of trade policy

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recently been, or will shortly be, eliminated or suspended. The EEC considered that it would, however, still be necessary to suspend the application of certain restrictions applied to imports from the USSR in order that previous trade flows can be continued.

14 A bilateral trade agreement including reciprocal MFN status was concluded with Czechoslovakia in April 1990. A joint resolution approving MFN status was adopted by the House and the Senate respectively on 17 and 24 October 1990.

15 A bilateral trade agreement including reciprocal MFN status was concluded in the Autumn of 1990. However, the agreement was not yet approved by both countries at the time of the preparation of this report.

16 A waiver of the so-called Jackson-Vanik Amendment to United States trade legislation, which requires the USSR to codify its liberalized emigration policies, was announced on 12 December 1990. This will make it possible for the United States, *inter alia*, to extend MFN treatment to the USSR.

17 In practice this means that many agricultural products became eligible for duty free access, whereas many industrial products where exempted from quota and ceiling restrictions on GSP treatment.

18 Bolivia, Costa Rica, Chile, Mexico and Venezuela.

measures in June 1990, including the termination of the suspension of issuance of import licensing (affecting 1200 items) and of company import quotas. Peru lifted import prohibitions imposed for balance-of-payments reasons and other NTMs such as licensing, in August and September 1990.

26. Recent efforts towards trade liberalization in other regions are also worth mentioning. As from January 1990 the Republic of Korea decided no longer to invoke GATT Art. XVIII B on which its Export and Import Public Notice system was based. The remaining restrictions will be progressively dismantled by mid-1997. The Consolidated Public Notice System, which brings together all regulations regarding import procedures contained in individual Acts, was improved through reduction of items subject to restriction, simplification of procedures for inspection and approval and elimination of import-related fees.[19]

27. Indonesia has adopted, as from 28 May 1990, a package of autonomous trade policy measures which includes *inter-alia*, reduction and elimination of non-tariff measures on some 350 products previously subject to import licensing, State trading arrangements or import arrangements. At the same date, customs duties on more than 2,500 items and import surcharges on 64 products were reduced. The Philippines further removed several items from the list of products requiring prior approval of the regulating agencies concerned. Thailand lifted licence requirements for imports of certain processed wood products and for certain motor vehicles. India liberalized imports of a wide range of capital goods by transfering additional items to open general licence.

28. Some African developing countries continued their efforts towards trade liberalization in 1990. The sytem of conditional import prohibitions in Egypt was reviewed with the intent of relying primarily on tariffs. In this regard, twenty-one items were removed in May 1990 from the list of products subject to conditional import prohibition. The General Import Programme of Morocco further liberalized imports. Kenya reduced tariff rates applied to imports of a great number of products and eased the granting of import licences for several lower priority items. Malawi further liberalized its import régime reserved to final users of the imported products. Cameroon reduced tariffs and removed some non-tariff measures with a view to gradually liberalizing its trade.[20] Tariff rates were revised, often downwards, in the Central African Republic, Côte-d'Ivoire, Senegal and Togo.

3. Anti-dumping and countervailing duty actions

29. The number of anti-dumping and countervailing duty actions initiated in the period July 1989 through June 1990 as a whole was slightly lower than in the preceeding 12 month period (see table I.9 of the Statistical Annex). After having decreased significantly in the period July 1988 through June 1989, the number of new cases remained practically unchanged in Canada and the United States. In recent years the number of outstanding cases has dropped dramatically in Australia.[21] While the number of outstanding cases in Canada has dropped over the last two years; it has remained constant in the EEC and the United States. However, the number of cases involving developing countries remained stable in Canada and increased in the EEC and United States. Consequently, the share of outstanding cases directed at developing countries increased in both countries.

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19 See: TD B 1283, *Information provided by States members of UNCTAD for the annual review by the Board on protectionism and structural adjustment.*

20 See: TD B 1283, *Ibid.*.

21 See: Gary Banks, *Australia's Anti-dumping Experience*, Canberra, Centre for International Economics, 1990.

B. Developments in trade legislation and major policies

1. Developments in market-economy countries

30. Under Article 4 to the Protocol to ANZCERTA (Australia-New Zealand Closer Economic Relations Trade Agreement) on acceleration of Free Trade in Goods, it was agreed that with effect from 1 July 1990 neither country would take anti-dumping action against goods originating in the territory of the other country. The Trade Practices (Misuse of Trans-Tasman Market Power) Act 1990 amended existing anti-dumping legislation in Australia, so that the agreement with New Zealand could be implemented. New Zealand changed the anti-dumping and countervailing law to put the agreement into force by the enactment of the Dumping and Countervailing Duties Amendment Act of 1990.

31. Canada amended its Special Import Measures Act 1984, which provides for the imposition of anti-dumping or countervailing duties, in order to make it consistent with the dispute settlement procedure established in Chapter 19 of the Canada-United States Free Trade Agreement.

32. In the United States the Customs and Trade Act of 1990, known as the "mini-trade bill", was signed into law on 20 August 1990. The legislative package included, *inter-alia*, provisions for extension of the Caribbean Basin Initiative (CBI II), changes of the Customs users fee, an expansion in the existing ban on log exports, miscellaneous tariff changes and reclassifications and authorization of MFN status for the former German Democratic Republic and Czechoslovakia.

33. The law made the Caribbean Basin Initiative (CBI II) permanent and provided for, *inter-alia*, a phased reduction of 20 per cent of import duties on certain leather articles from CBI countries and for duty-free treatment for products (other than textiles, apparel or petroleum products) that are assembled in CBI countries entirely from US components or ingredients; it extended for one year duty-free imports of ethanol as long as a certain proportion of value was added in a CBI country; it allowed immediate eligibility for Nicaragua under the CBI and GSP. This law also directed that imports from CBI countries be counted separately by the US International Trade Commission when making injury determinations in trade-remedy cases and directed the USITC to consider recommendations for changes in the CBI rules of origin.

34. The Customs and Trade Act also includes provisions to revise the Customs merchandise processing fee (customs user fee) in order to bring it into compliance with the conclusions of the GATT panel report adopted on 2 Feb. 1988 that found the original *ad-valorem* fee's structure to be illegal. The revised fees were effective from 1 October 1990. Exemptions were provided for CBI, least developed countries, insular possessions, most entries under Chapter 98 of the Harmonized Tariff Schedule and Canadian FTA goods. The law further directed the Customs Service to determine its actual costs for processing various types of imports and to report to Congress. This implies the possibility for further adjustments so that the fees would be in closer conformity with the GATT panel report.

35. The US House of Representatives and the Senate approved a compromise version of the Farm bill which amended many aspects of the US agricultural policy, including trade programmes, setting agricultural policy for a five-year period starting in 1991. The respective versions of the bill were approved by the Senate on 27 July and by the House of Representatives on 1 August. The compromise version of the bill would cut US $ 13.6 billion from agricultural programmes, but did not retain a controversial provision that would have banned the export of pesticides that were banned for use in the United States. Lawmakers in the Congress were to reconcile also provisions related to: Uruguay Round agricultural negotiations; agricultural trade strategy; sugar import quotas; food aid; wood products; inspection fees; country of origin labelling; debt forgiveness; and restrictions on imported fruits.

36. After having received a formal request from Mexico's President for the start of free-trade negotiations, the President of the United States transmitted to the Congress his notice of intent to negotiate a bilateral free trade agreement with Mexico and endorsed Canada's participation in the negotiations. The formal notification triggers the "fast-track" provision in US trade law, which gives the President authority to enter the negotiations unless the Congress disapproves within 60

legislative days.

37. In June 1990 the Swedish Parliament decided to introduce a new agricultural policy which will be put into effect on 1 July 1991, with a transition period of about five years. The main theme of this policy is that agricultural production will be in principle be subject to the same conditions as branches in the industry sector. The decision implies in principle the abolition of internal regulations including export subsidies.[22]

2. Developments in the USSR and in Eastern Europe countries

38. Czechoslovakia is now fully committed to liberalizing its foreign trade and integrating the country fully in the international trading and monetary systems. Its customs régime (Decree No.228/1988) is based on the Harmonized System. The Foreign Exchange Law, which came into force in December 1989, introduced the provision of foreign exchange self-financing and allowed the enterprises to retain most of their foreign exchange earnings. Amendments to the Law 42 on Economic Relations with Foreign Countries in mid-1990, largely swept away the monopoly of the State-owned foreign trade organizations, giving the right to all Czechoslovak companies and individuals the right to trade internationally in goods which they produce. A new version of this law is being drafted, which would give, (most probably from the begining of 1991) the companies registered in the enterprises register, full right to trade internationally in any product, except arms and some strategic products which will still require a special license.

39. A bilateral trade agreement between Czechoslovakia and the United States was concluded on 12 April 1990. This agreement, which has been endorsed by a joint resolution by the two houses in the US Congress in October 1990 and which would become effective after signature into law by the President of the United States and approval by the Czechoslovak Parliament, includes provisions for reciprocal MFN trade treatment as well as provisions on dispute settlement, intellectual property protection and business facilitation. A separate investment agreement is being negotiated.

40. In Hungary, the basic legislation allowing Hungarian enterprises, joint ventures and foreign companies domiciled in Hungary to work under market conditions and to engage themselves in foreign transactions, had already been promulgated. Most of the Government's aims and policies contained in the three-year National Renewal Programme adopted by the Government at the end of September 1990, have a direct impact on the operational conditions and the competitiveness of all enterprises in Hungary. These include, *inter-alia*, a further liberalization of licensing requirements in foreign trade. It is envisaged to increase the percentage of license-free convertible currency imports from 70 per cent in 1990 to 80 per cent in 1991.

41. Recent legislation in Poland having a direct impact on its foreign trade relate to customs tariffs and currency. The Currency Law of February 1989, amended at the end of that year, legalized foreign currency transactions by Polish citizens, allowed exporters to be owners of their foreign currency revenues and facilitated the introduction of the internal convertibility of the Zloty from the beginning of 1990. The customs tariff, based on the Harmonized System has been modified by a new customs regulation which entered into force on 1 January 1990. A number of tariff rates were modified during 1990. The control of commercial transactions and customs procedures was tightened in mid-1990.

42. At the beginning of 1990 Poland formally requested renegotiation of its terms of accession to GATT. In Romania the economic programme of transition towards a market economy aims, *inter-alia*, at liberalizing prices and foreign trade.

43. In the USSR the Basic Guidelines for the Stabilization of the National Economy, adopted by the Supreme Soviet at the end of October 1990, *inter alia*, considerably reduce State control of foreign trade. The Basic Guidelines as regards external economic activity, are based on a single customs territory, currency system, investment arrangements and a common external economic policy whilst enlarging the powers of the Union Republics in these fields. During the transition to a market economy and while denationalizing and decentralizing this sector, external commercial

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22 See: TD B 1283, *Ibid.*.

operations will be handed over to the enterprises whose freedom to carry out business operations will be guaranteed, leaving the State bodies to concentrate on regulating and promoting these operations. Sectoral organizations (FTOs) which used to play a direct role in many fields of external economic activity, will become intermediaries.

Chapter III

ASSESSMENT OF OFFICIAL TRADE INTERVENTION

44. The secretariat has continued to update the information contained in the UNCTAD Data Base on Trade Control Measures. Particular efforts have been devoted to establish computerized records expressed in the Harmonized System Nomenclature, particularly for the major trading nations. Such records are now available for the developed-market economy countries and a number of major developing country importers.

45. Through decision 384 (XXXVII) the Trade and Development Board requested the secretariat

> "... in connection with the efforts to promote dialogue within UNCTAD on the interlinkages between environmental and trade policies, to adjust the UNCTAD Trade Control Measures Information System to monitor environmental regulations for possible protectionism and to monitor non-tariff measures which have a bearing on the environment."

46. The secretariat has compiled information on government regulations and practices that may distort international trade. In the analysis on official trade intervention, priority has been given to measures which introduce differential treatment between imports and domestically produced goods. Standards and regulations have not been included in such analysis.[23] Therefore, there has been no need to collect information on such measures in the context of the annual review of the problem of protectionism.

47. However, some of the country files in the data base already contain information on such measures, to permit greater transparency in international trade.[24] The codification of NTMs has been revised recently *inter alia* with a view to identifying more accurately measures defended on environmental and other non-commercial grounds.[25] For instance, prohibitions or licensing requirements which are applied with the stated purpose of protecting public health, safety, wildlife or the environment, are being entered under specific codes.[26] The Secretariat is increasing its efforts to collect information on environmental regulations. It would be very useful if member States could provide the secretariat with environmental regulations and the corresponding product coverage in Harmonized System (HS) nomenclature.

48. For the assessment of the extent of trade intervention, the secretariat has changed the base year to 1988, the year in which a large number of countries adopted the HS nomenclature.[27]

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23 Although the secretariat makes no *a priori* judgement as to the intention of NTMs, their restrictiveness and their conformity or otherwise with international trade rules, certain prohibitions and licensing requirements affecting specific prodcuts categories such as dangerous and hazardous substances have normally been excluded from such analysis. In document TD B 1267, paragraph 46, the secretariat states that "they (environmental measures) may be justified in some cases, but in others they may be the pretext for protectionst measures". While encoding information in the data base it may not be possible "to distinguish between pretexts and valid cases". However, the ongoing task of the secretariat would be to provide Governments with information to help them assess the justification of such measures.

24 In its current status, the Data Base includes only trade measures which are applied on imports at the border. Public regulations which may affect imported goods after customs clearance, are not included in the Data Base. A number of environmental policies, such as fiscal policies, will not be considered in the Data Base as currently constructed.

25 See: UNCTAD DDM Misc. 18

26 These codes are also being used when the stated purpose of the regulations is not known, but it can clearly be assumed that measures have been taken with a view to protecting the environment, given the character of the product in question.

27 The secretariat staff is further backdating certain records for analytical purposes.

49. The calculations of trade intervention indicators[28] are based on the observation of over one million trade flows into 10 developed countries and the EEC.[29] About 15 per cent of these trade flows were affected by one or more selected NTMs in 1990 (The NTMs considered in the calculations are summarized in table I.15). In value terms, it was estimated that more than 18 per cent of all non-fuel imports were subject to one or more of the selected non-tariff measures in 1990 (more than 12 per cent if the "narrow" selection of non-tariff measures is considered).[30]

50. The trend analysis is based on a rather short period of only three years (1988-1990). Table I.10 of the Annex shows that the share of trade flows affected by non-tariff measures (frequency index) declined slightly in clothing, fuels, chemicals and, especially, iron and steel. From 1988 to 1990 the trade coverage ratio (broad definition) increased by nearly one percentage point. However, this figure is heavily influenced by one single trade action.[31] An increase of the NTM trade coverage ratio is observed for the group of all food items and for the manufactures sector as a whole as well as in leather,[32] mainly due to anti-dumping and countervailing duty actions. The increase in the TCR of the "broad" group of NTMs seem to indicate that the trade coverage of the stock of outstanding anti-dumping and countervailing duty actions has increased from 1988 to 1990, which would be in line with the findings presented in section A.3 of chapter II and table I.9 of the Annex. However, as the trade coverage of anti-dumping and countervailing duty actions is difficult to calculate from national trade statistics this result has to be interpreted carefully.

51. It can be observed from Table I.11 in the Annex that, when a "narrow definition" of NTMs is used in the calculations, there is a slight decrease of the coverage ratio, resulting from liberalization in the three sectors with the highest level of governmental non-tariff trade intervention, *i.e.*, food and live animals,[33] clothing and iron and steel.[34]

52. Table I.12 shows how different country groupings were affected by the application of non-tariff measures. Imports from the developing countries and China are relatively more affected by the application of non-tariff measures than those from the group of developed market-economy countries, particularly in sectors where they have acquired a competitive advantage, *e.g.* textiles and clothing, leather and footwear. The share of imports from developing countries affected by NTMs is also high, compared to other country groupings, in agricultural raw materials and animal and vegetable oils. The incidence of NTMs in imports from USSR and Eastern European countries was still relatively high in 1990. It declined for Hungary and Poland, due to the suspension of specific quantitative restrictions applied in EEC member States effective 1 January 1990. Further steps to dismantle NTMs on imports from the USSR and countries in Eastern

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28 The trade coverage ratio indicates the percentage share of the value of imports covered by selected NTMs. Trade coverage ratios are computed at the national tariff line level and then aggregated, using trade weights of a fixed base year. To arrive at the frequency index, the number of trade flows subject to selected non-tariff measures is expressed as the percentage share of the total number of trade flows. The number of trade flows for each importing country is the number of national tariff lines times the number of trading partners in which imports originated at each tariff line in the base year.

29 As certain NTMs in the EEC are applied at the national level, the number of import flows into each member State is calculated separately and then added up across member States. For this reason imports into the EEC alone involve more than 500 thousand transactions.

30 Three groups of non-tariff measures are defined for analytical purposes. The first group (referred to as "all selected NTMs") includes a broad range of NTMs, including para-tariff measures (tariff quotas, increased tariffs for safeguard or retaliatory purposes), variable levies, countervailing and anti-dumping actions, quantitative restrictions (including prohibitions, quotas, non-automatic licensing, State monopolies, 'voluntary' export restraints and restraints under MFA and similar textile arrangements), import surveillance (including automatic licensing) and price control measures. The second group ("narrow definition") includes the same measures except for para-tariff measures, countervailing and anti-dumping actions and import surveillance. A third group of NTMs consist of quantitative restrictions only.

31 An anti-dumping action involving U.S. imports of limousines originating in Canada (the action was terminated in early 1990). The trade coverage of this action may be considerably overstimated.

32 Reflecting a countervailing action by the United States against imports of leather from Argentina, initiated in March 1990.

33 In the United States, VERs with Australia and New Zealand concerning products covered by the Meat Import Law were not renewed after October 1988. Japan terminated import quotas for certain agricultural products in both 1988 and 1989. In 1988 the EEC terminated VERs affecting imports of apples from countries in the southern hemisphere. Elimination of sugar import quotas by the United States is not yet reflected in the table, as these were still in force until end September 1990.

34 The United States terminated a safeguard action (increased tariffs and quotas) on specialty steel effective 30 September 1989. In addition, the EEC did not renew VERs with the Republic of Korea and Venezuela.

Europe undertaken by some countries in the course of 1990 are not yet reflected in the indicators.[35]

53. It must be noted that the trade coverage ratios presented in tables I.10 through I.12 are lower than those for the same period presented in previous reports. There are three reasons to explain this. First, as was discussed in chapter 2 of TD/B/1126, the incidence of NTMs tends to be higher in sectors with relatively slow import growth. Therefore, moving the base year forward in time may by itself have a downward bias on the trade coverage ratio (the share of imports affected by NTMs). Second, a few measures which were included in the CCCN data base previously used have not been transposed to the Harmonized System data base.[36] Third, for most countries the HS tariff schedules contain a much larger number of items than the schedules using previous nomenclatures.[37] The new nomenclature thus permits a more precise definition of tariff items affected by NTMs.[38]

54. The quantitative assessment also refers to NTMs applied in a small group of developing country/territory markets for which HS trade statistics were available: Brazil, the Republic of Korea, Hong Kong, Malaysia, Mexico, Thailand and Singapore (the NTMs considered in this analysis are summarized in table I.16 of the Statistical Annex). The calculations are exactly the same as used traditionally for developed countries. The value of total imports by these six countries in 1988 amounted to some US $ 230 billion or 40 per cent of all developing country imports. Therefore the indicators shown may not be fully representative for the group of developing countries as a whole. However, some conclusions may be drawn from the indicators shown in tables I.13 and I.14 in the Annex, which seem to confirm some of the findings of an earlier study.[39] First, unlike in many developed market-economy countries, NTMs in developing countries tend to be applied on a MFN basis without discriminating against specific groups of trading partners. Selective NTMs, such as VERs and MFA restrictions are not applied, although the Republic of Korea and Mexico have used anti-dumping actions to some extent. Second, NTMs are less sector-specific than in DMECs. This conclusion may have to be qualified for certain countries which are going through liberalization processes with specific time schedules for different sectors.

Chapter IV

SELECTED ISSUES

A. Tariffs

55. Document TD/B/1126 produced some evidence that, already in the mid-1980s, in some developed market-economy countries the tariff treatment of the developing countries as a whole was less favourable than that afforded to the other developed countries. There are a number of reasons to believe that preferential treatment for developing countries has been further eroded in recent years. The principal developments since then in the context of tariffs were (a) the new free trade agreements between developed market-economy countries; (b) the granting of GSP status to

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[35] The trade intervention indicators for a given year are calculated taking into account the selected measures in effect during all or part of the year. Therefore, the removal of any measure would be reflected by the indicators in the subsequent year.

[36] This applies particularly to automatic licensing requirements for products listed in Annex II to Regulation (EEC) 288/82.

[37] For instance, the HS Tariff Schedule of the United States contains around 10,000 8-digit tariff lines, compared to 5000 tariff lines used in the 5-digit TSUSA nomenclature.

[38] This may be particularly important for such measures as anti-dumping and countervailing duty actions which normally affect narrowly defined product categories.

[39] See: R. Erzan, H. Kuwahara, S. Marchese and R. Vossenaar, *The profile of protection in developing countries*, UNCTAD Discussion paper No. 21.

countries in Eastern Europe; and (c) the exclusion of certain major developing country exporters of manufactured products from the GSP schemes of certain preference giving countries.[40]

56. With the exception of Japan all DMECs which grant GSP and other tariff preferences to developing countries also participate in arrangements providing for the exchange of tariff preferences beween two or more of them (see table I.17 of the Statistical Annex). Imports which benefit from tariff preferences within the framework of such agreements tend to account for a significant share of total imports from other developed countries, often exceeding the share of GSP or other preferential trade in total imports originating in developing countries. Consequently, the trade weighted average duties applied to imports from other developed countries are often lower than the trade weighted duties applied to imports from developing countries. This is the case particularly in EFTA countries, which provide almost complete duty-free treatment to each other as well as to the EEC in industrial products. As trade with these countries is very important, only a small proportion of imports from developed countries receives MFN treatment.[41] In North America, bilateral trade between Canada and the United States accounts for an important share of all dutiable imports of each of the two countries.

57. In the United States, the value of imports which are entitled to preferential tariff treatment as a share of all MFN-dutiable imports is roughly the same for developing and as for developed countries (see table I.18).[42] As Canada receives tariff preferences on almost all items, whereas products such as steel, textiles and footwear are excluded from the GSP schedule of the United States, developing countries as a whole receive less preferences than other developed countries in these products categories.

58. In the EEC, the value of imports which in principle are entitled to tariff preferences as a share of total imports is much higher for developing countries than for other developed countries. However, for certain product categories, such as steel and footwear, other developed countries receive relatively more tariff preferences (see table I.19 in the Annex).

B. Changing market access conditions for imports from the USSR and countries in Eastern Europe.

59. OECD countries have taken various steps to improve conditions of access to their markets for imports from the USSR and countries in Eastern Europe, with a view to supporting their economic reforms and to strengthening their integration into the international trading system. This section gives a summary of recent changes in tariff treatment and the application of non-tariff measures in the major OECD markets. Finally, the possible trade creation and trade diversion effects of granting GSP preferences to Hungary and Poland by the EEC and the United States are estimated, using the UNCTAD Trade Policy Simulation Model.

60. Table I.20 of the Statistical Annex summarizes market access conditions for Bulgaria, Czechoslovakia, Hungary, Poland, Romania and the USSR. Four of these countries (Czechoslovakia, Hungary, Poland and Romania) are GATT contracting partners. Although most OECD countries have different tariff rates for GATT contracting parties and other trading part-

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40 In addition, a disproportionate part of NTMs applied in developed countries is directed against developing countries. This is not only due the combined effect of selective NTMs and the structure of developing country exports to developed countries, but also to the existence of special arrangements between developed countries. For instance, EFTA countries tend to exempt each other and the EEC from licensing requirements for certain products. Australia and New Zealand no longer apply NTMs to each other. The incidence of NTMs in trade between Canada and the United States is quite low.

41 See, for instance, the GATT *Trade Policy Review on Sweden, 1990*.

42 The estimated trade weighted average tariff for all transactions originating in developing countries is compared to the average tariff on imports from developed countries. Wherever applicable the tariff averages are calculated on the basis of prefential duty rates, taking into account product coverage and beneficiary lists of each scheme. If a certain transaction is not eligible for preferential treatment, either because the product in question is excluded from any preferential schemes or because the specific developing country supplier is not a beneficiary of such schemes, the tariff revenues are calculated on the basis of the MFN rate of duty. Tariff lines with specific or combined rates were excluded from the calculations.

ners, in practice all countries except the United States provide MFN status to the non GATT countries in Eastern Europe, through bilateral agreements.

61. The major obstacle to the market of the United States used to be the tariff status. In 1989 only two countries, Hungary[43] and Poland,[44] had MFN status. Imports from other countries were subject to the Column 2 Rate of Duty, which is normally substantially higher than the MFN rate of duty. In 1990 the United States concluded agreements with Bulgaria and Czechoslovakia which include MFN tariff treatment.[45] In June 1990, the United States and the USSR concluded a trade agreement. The USSR will receive MFN status if it meets the conditions with regard to emigration policies.

62. A number of preference giving countries have extended GSP benefits to countries in Eastern Europe. Austria has granted GSP status to Hungary, effective 1 January 1989. Hungary and Poland now receive GSP benefits in the EEC, the United States, Japan and Austia. The EC Commission, co-ordinating actions by a group of 24 donor countries with a view to strengthening economic relations with countries in Eastern Europe, has proposed that favourable tariff status should be provided also to Czechoslovakia, Bulgaria and Romania.

63. Important progress has also been made in removing quantitative restrictions on imports from USSR and Eastern European countries (see chapter II). In addition, the EEC allowed larger quantities of textiles to be imported from Hungary and Poland by increasing the quota allocations in the framework of bilateral MFA agreement, effective March 1990, and increased steel import quotas for Bulgaria, Czechoslovakia, Poland, Hungary and Romania. The EEC and the USSR concluded a bilateral textile agreement, leading to a relaxation of previous import restrictions on certain textile products. The United States increased the quantities of steel products that may be imported from Hungary and Poland under the VERs concluded with these countries.[46]

64. Changes in access conditions for Hungarian and Polish export products with regard to tariffs and NTMs are analysed in some more detail.[47]

65. Due to the high portion of agricultural products, covered by the Common Agricultural Policy and, to a lesser extent, steel and textile products in Hungarian exports to the EEC, the incidence of Community wide NTMs is higher than for Poland. Therefore, products for which specific quantitative import restrictions in EEC member States were the only non-tariff measure accounted for a smaller share of Hungarian exports than of Polish exports.

66. Estimates for Hungary would indicate that gains in terms of increased export revenues on GSP items, considering current trade flows, would be quite modest (around 14 per cent in both the EEC and the United States). This could be explained by the high proportion of agricultural products in GSP items imported from Hungary.[48] Such items normally have small preference margins and low price elasticities of import demand. For Poland possible gains in terms of increased exports to the EEC market would be more important, exceeding 20 per cent. A limitation of the simulation model is that it estimates changes in current trade flows. GSP should be a stimulus to export diversification and the potential benefits of exporting new export products may add significantly to the increase in revenues on current export articles.

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43 In October 1989 the President reported to the Congress that Hungary was in full compliance with the freedom-of-emigration requirement of section 402. The determination released Hungary from the waiver procedure that had made its status subject to annual review (USITC: Trade Between the United States and the Nonmarket Economy Countries During January-March 1990, page 2. (USITC publication 2302)).

44 MFN treatment was suspended in October 1982, but restored in February 1987.

45 The agreement with Czechoslovakia was concluded in April, 1990. A joint resolution approving MFN status was adopted by the House and the Senate respectively on 17 and 24 October 1990. The agreement with Bulgaria was not yet approved by both countries at the time of preparing this document.

46 On 12 December 1989, the quota allocated to Hungary was increased by two-thirds and to Poland by 44 per cent (USITC Operation of the Trade Agreements Program, 41st report, 1989, page 10).

47 Such changes are exemplified in tables I.21 through I.24, showing tariff and non-tariff treatment given to the 45 leading import products from each of these countries in the EEC and US markets. Estimates of the possible gains in export revenues, after having been granted GSP status in the EEC and the United States are also indicated.

48 Hungarian exports to the United States are heavily concentrated in agricultural products, textiles, clothing and steel products. Therefore the average tariff rate is quite high, while a relatively high share of leading products are excluded from GSP. Only 15 out of the 45 leading export products are entitled to GSP treatment.

C. Agriculture.

67. This section reviews briefly trends in the international market for agricultural products, the nature and extent of policy measures affecting agricultural trade, and some implications of trade liberalization, particularly for developing countries.

68. Agricultural products, including temperate zone and tropical products, are a major component of international trade. World trade in agricultural products grew by 5 per cent in 1989 to reach $410 billion. Food products accounted for nearly 80 per cent of this value and agricultural raw material for the remaining 20 per cent.

69. Whereas developed market-economy countries continue to dominate world trade in agricultural products, the developing countries remain highly dependent on the production and export of such products. For example, in 1988, whereas agriculture accounted for only 2.5 per cent of gross domestic product of countries of the Organisation for Economic Co-operation and Development (OECD), it accounted for 10 per cent in Latin America and the Caribbean, 22 per cent in East Asia, 33 per cent in South Asia and 34 per cent in sub-Saharan Africa. As regards employment, in 1988 more than 60 per cent of the labour force of developing countries derived their income from the agricultural sector, compared with 6 per cent in the developed market-economy countries. This much greater dependence on agricultural production in developing countries is accompanied by a high dependence on agricultural exports. The share of agricultural products in total merchandise exports ranges from 50 per cent to 100 per cent for the majority of developing countries.

70. While developing countries are highly dependent on exports of tropical agricultural products, they are also dependent as a group, with a few exceptions, on imports of temperate (competing zone) agricultural products, that is, basic foodstuffs. For example, imports into developing countries of the four food categories (cereals, dairy products, meat and edible oils) averaged about $30 billion annually in 1986-1988, with cereals alone accounting for half of this amount. Total food imports of developing countries, over the same period, averaged nearly $50 billion annually.

71. The international market for agricultural and tropical products is affected by a variety of policy measures applied by Governments. These measures include border protection (tariffs, tariff escalation and non-tariff measures) to limit import access, internal support policies (subsidies in various forms to domestic producers) the effect of which is to raise domestic production higher than it would otherwise be, thus reducing domestic demand for imports or leading to higher export availibility, and export subsidies (which distorts competition among exporting countries). While policies falling into one or more of these categories are applied by many Governments, those applied in the markets of the industrialized countries, because of the importance of these markets in international trade, have the greatest impact on the world market.

72. Estimates of producer subsidy equivalents (PSEs) for major farm commodities by the OECD secretariat indicate that transfers to farmers in 1987, at $173 billion, was the highest of the decade. In that year producers obtained almost 50 per cent of their agricultural income from these transfers. Since then, there have been a relative decline in transfers, to $160 billion in 1988 and $141 billion in 1989. This still leaves, however, transfers to farmers in OECD countries above their already high level for the first half of the 1980s (an average of around $100 billion for 1979-1985). In absolute terms, the EEC ($53 billion), Japan ($34 billion), and the United States ($32 billion) account for the bulk of farm support in the OECD area. On a percentage basis Switzerland, Norway, Finland and Japan have the highest rates of assistance (over 70 per cent). In contrast, New Zealand (5 per cent) and Australia (10 per cent) have the lowest rates.[49]

73. Agricultural support policies, particularly those which are based on market price support, raise prices to consumers considerably above the levels that would prevail in the absence of policy interventions. The consumer subsidy equivalent (CSE) for OCED countries rose from $66 billion in 1979-1985 to $132 billion in 1987. In 1988 the CSE fell to an estimated $122 billion, almost

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[49] See: OECD, *Agricultural Policies, Markets and Trade: Monitoring and Outlook 1990*, (Paris,1990).

exclusively on account of the increase in international prices that reduced the gap between domestic consumer and import prices. Provisional figures for 1989 suggest a further decline in the CSE, to $104 billion, due to a combination of lower internal and higher world prices.

74. Because PSE and CSE estimates neither cover all agricultural products nor include all transfers due to agricultural policies, they do not by themselves provide a complete picture of all the transfers generated by agricultural policies. The overall transfers from taxpayers (net of budget receipts from tariffs) and consumers (through higher prices) was an estimated $251 billion in 1989. Although this was lower than the peak value of $290 billion recorded in 1987, it was still above the already high level for the first half of the 1980s.[50]

75. Agricultural support policies often include export measures, involving significant budget outlays, such as direct export subsidies and credits and other export aids. Export subsidies have become a major source of disputes in agricultural trade in recent years because of their use to dispose of production in excess of domestic requirements on world markets. Because subsidized exports can lower world market prices and can be used to capture market share, they inflict income losses on non-subsidized exporters. However, they provide income transfers to importing countries of agricultural products benefiting from subsidies. The share of export subsidies in the 1986-1988 average levels of agricultural support (in terms of PSEs) in six OECD countries (including Australia, Canada, EEC, Japan, New Zealand and United States) ranged from 0.3 per cent for New Zealand to 43.7 per cent for the EEC.[51] In 1989, export subsidies continued to be utilized by a number of OECD countries, including the EEC, the United States, Switzerland, Norway, Austria, Finland, Canada and Sweden, for particular agricultural exports.

76. The Uruguay Round of multilateral negotiations under the auspices of GATT has provided the framework over the past four years in which efforts have been made to liberalize international trade in agricultural and tropical products. At the launching of the Round, Ministers agreed, *inter alia*, that the negotiations on tropical products should aim at the fullest liberalization of trade in those products, including in their processed and semi-processed forms. Both tariff and all non-tariff measures affecting trade in those products were to be covered in negotiations. In recognition of the importance of trade in tropical products to a large number of developing countries, they also agreed to give negotiations in this area special attention, including in the timing of the negotiations and in the implementation of the results.

77. Offers of tariff concessions on tropical products (as at the end of July 1990) by major industrialized trading countries (including Australia, Austria, Canada, EEC, Finland, Japan, New Zealand, Norway, Sweden, Switzerland and the United States) suggest the following direct trade effects:

- The improvement in market access corresponding to these offers would create additional trade (imports by the markets), in the products covered, amounting to about US $ 746 million or about 3 per cent of the 1986 import value of such products by those markets;

- Only a third of the additional imports created (that is, $245 million) would come from developing countries, representing only a 1.7 per cent rise in their exports to those markets of the products covered. The remainder of the additional trade would accrue to the industrialized countries themselves;

- On an aggregate regional basis, the African region is the only one among the developing regions that experiences a net loss (approximately US $ 118 million), about 3 per cent of its 1986 export value of covered products.

78. These results are explained by the fact that offers are made for the most part on an MFN basis. Therefore, in so far as certain products are also produced by industrialized countries (for example, processed tropical products) liberalization in the tropical products sector will bring benefits not only to the developing countries. Furthermore, to the extent that developing countries already enjoy preferential tariff treatment on such products, liberalization on an MFN basis implies an erosion of preference margins; hence trade losses can be expected. In fact, for least developed countries that enjoy better than GSP treatment in some markets, even liberalization on a

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50 See: OECD, *op. cit.*

51 See: OECD Economic Studies, *Modelling the effects of agricultural policies*, No. 13, Winter 1989-90, table 2, p.137.

GSP basis would not bring additional trade benefits. A similar situation would apply to ACP countries with respect to the EEC market.

79. As concern agriculture more generally, the Punta del Este Declaration specifies that negotiations were to "aim to achieve greater liberalization of trade in agriculture and bring all measures affecting import access and export competition under strengthened and more operationally effective GATT rules and disciplines". For the first time in the long history of trade negotiations in GATT, negotiations on agriculture were given a central role.

80. The proposals of the United States, the European Community, the Cairns Group and Japan dealing with internal support, border protection and export competition, of the net food-importing developing countries and of those countries calling for due recognition of the importance of non-trade concerns (food security, environmental protection, development dimension, etc.) have been the main focus of attention in the negotiating group on agriculture. Negotiations on the amount and duration of the substantial and progressive reductions in support and protection, agreed as the objective of the negotiations at the mid-term, proved to be the most difficult with some countries proposing 75 to 90 per cent reductions over a ten-year period while others proposing a 20 to 30 per cent cut over a five-year period. Also, the appropriate accommodation in the reform process of special and differential treatment for developing countries, the situation of net food-importing developing countries and non-trade concerns such as food security, has been of great interest to a number of countries.

81. Several studies have been undertaken of the possible impact of the reform process in agriculture.[52] In general, these studies suggest that one overall effect of liberalization in this sector would be an increase in the prices of basic food products, leading to higher terms of trade for exporters and lower terms of trade for importers of these products. As far as concerns developing countries, the net exporting countries will clearly benefit from higher prices, which would undoubtedly improve the profitability for the farming sector in some countries and reduce government expenditures on agricultural income support programmes in others, particularly the large exporters. More remunerative prices in the long run could also contribute to making domestic food production in food-deficit developing countries more attractive, provided such prices are passed on to the farmers and are complemented by institutional and infrastructural improvements. While a rise in food prices could be beneficial in the long run, in the short run it would bring hardship, particularly to the poor. In the short run, high food prices would continue to increase pressure on the balance of payments of many food-deficit countries with serious consequences on the well-being of the poor, whose food intake is already inadequate. Therefore, it would be important that continued efforts be made in the developing countries to increase production of basic food wherever this is economically possible.

D. Market access for African countries

82. This section examines market access conditions for sub-Saharan African countries in the markets of the EEC, the United States and Japan.

83. The Fourth Lomé Convention was signed by the EEC and 69 developing countries of the African, Caribbean and Pacific (ACP) on 15 December 1989 for a period of ten years ending 1 March 2000. It continues to grant unrestricted duty-free access, on a non-reciprocal basis, for industrial products and many agricultural products and to provide ACP countries with funds for development aid. The system of stabilization of export earnings from agricultural commodities (STABEX) and the special financing facility for mining products (SYSMIN) have been reinforced.

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52 For example, see: K. Anderson and R. Tyers, "Liberalizing OECD Agricultural Policies in the Uruguay Round: Effects on Trade and Welfare", *Journal of Agricultural Economics*, 39 (2), May 1988; K. S. Parikh, G. Fischer, K. Frohberg and O. Gulbrandsen, *Towards Free Trade in Agriculture*, Amsterdam: Mortimers Nijhoff for IIASA, 1988; V.O. Ronningen and P. M. Dixit, *Economic Implications of Agricultural Policy Reform in Industrial Market Economies*, ERS Staff Report, Washington D.C.: United States Department of Agriculture, August 1989; I. Goldin and O. Knudsen, eds., *Agricultural Trade Liberalization: implications for developing countries*, Paris: OECD, 1990; and UNCTAD/UNDP/WIDER, *Agricultural Trade Liberalization in the Uruguay Round: Implications for Developing Countries*, New York: United Nations, 1990.

The new agreement provided better market access conditions for about 40 agricultural products, such as sorghum, millet and rice. In addition, improvements were made through relaxation of rules of origin and trade facilitation in services.

84. Almost half of the value of exports of African ACP countries to the EEC are duty-free on a MFN basis and are, in principle, not affected by the Uruguay Round Negotiations.[53] Tariff concessions on other products will result in the loss of preference margins and possible trade diversion away from ACP countries to other suppliers. In the area of tropical products, the Montreal mid-term meeting contained negotiated contributions, which were implemented on a provisional basis. For the African countries, EEC tariff concessions resulted in loss of preference margins on some important export products such as coffee, coffee extracts, cocoa, guavas, vanilla beans, pepper and certain roots. The revised offers of tariff concessions in tropical products as well as offers made in other negotiating groups, such as natural resource based products would result in some further erosion of preference margins and a net loss of export revenues.[54]

85. In the area of non-tariff measures, African countries would benefit from the proposed reduction of internal taxes on a number of tropical products in some EEC member States.

86. In the United States, the possible net impact of tariff concessions on export earnings for African countries is less clear. Around 75 per cent of the value of imports from Africa enters the United States market duty-free, and are therefore not affected by the US tariff concessions. The only tariff preferences granted to African countries are those under GSP. The GSP scheme excludes a number of products of export interest to Africa.[55] Only 50 per cent of the value of MFN dutiable imports is eligible for GSP preferences. In certain sectors, trade creation as a result of tariff concessions might outweigh negative trade diversion following erosion of tariff preferences. However, a large part of imports excluded from GSP are in the textiles and clothing sector. Imports from the major African exporter, Mauritius, are subject to quota and other restrictions. Other imports excluded from GSP are in some basic metals, particularly unwrought zinc. However, the MFN rate of duty is quite low. In the area of NTMs, a major development is the transformation of sugar quotas into tariff quotas.[56]

87. In Japan, one third of all imports from sub-Saharan Africa, in value terms, enter duty-free on a MFN basis. Around 10 per cent is subject to the MFN rate of duty and may benefit from tariff concessions. The remaining 56 per cent of imports receive tariff preferences, either at GSP or LDC rates. The erosion of preference margins might therefore be important and result in losses of export revenues in products which are produced both in developing and developed countries. Revised offers of tariff concessions in March and November 1990 extended the products coverage, resulting in an average reduction in MFN rates of duty of around 40 per cent. In the area of natural resource based products, African countries would benefit from tariff concessions in the area of fish, as most items imported from Africa are dutiable on a MFN basis, at rates ranging from three to five per cent, while most items are excluded from GSP and LDC treatment.[57] In the area of minerals and metals, tariff concessions would probably result in a net loss of export revenues due to erosion of preference margins. The principal foresty products exported by countries in sub-Saharan Africa enter the Japanese market duty-free on a MFN basis.

88. Considering the tariff offers by major industrialized countries as at the end of July 1990, on an aggregate basis, the African region is the only among the developing regions that experiences a net loss in export revenues, both in tropical products and natural resource based products.

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53 In its offer on agriculture, the EEC proposed in November 1990 to open tariff quotas on a number of items, in the framework of rebalancing, resulting in an increase in corresponding MFN rates of duty. As ACP imports would not be subject to tariff quotas, African countries would receive larger preference margins. This system would affect certain products of export interest to Africa, particularly molasses, oil cakes, and groundnut oils.

54 However, by mid Novemebr 1990, no offers had been made on fish items, bananas, beans, groundnut oil, sugar, molasses, pineapples, pineapple juice and tobacco.

55 For instance, fish, coffee, tea, vanilla, beans, extracts of tropical plants, and cocoa (except cocoa paste).

56 See chapter II. Under the new system, quotas under the primary rates were allocated to African countries, as follows: Congo (7,730 metric tons), Côte d'Ivoire (7,730 mt), Gabon (7,730 mt), Madagascar (7,730 mt), Malawi (16,592 mt), Mauritius (19,910 mt), Mozambique (21,659 mt), Swaziland (26,547 mt), Zimbabwe (19,910 mt.).

57 An important exception is octopus (*Octopus spp.*). The MFN-rate of duty is 10 per cent. The GSP rate is 5 per cent, while imports from LDCs (particularly Mauritania and Gambia) are duty free.

PART TWO

MAJOR STRUCTURAL DEVELOPMENTS IN THE WORLD ECONOMY AND EXPORT PROSPECTS OF DEVELOPING COUNTRIES

Chapter I

STRUCTURAL CHANGE AND ECONOMIC INTEGRATION IN EUROPE: RECENT DEVELOPMENTS AND IMPLICATIONS FOR EXPORTS FROM DEVELOPING COUNTRIES

89. Political and economic changes and progressing economic integration and co-operation in Europe are likely to assume a new dimension and may lead eventually to the formation of a wider "European Economic Space". The EEC has been enlarged by its new southern member countries and a single market will be formed by the end of 1992. In parallel, the EEC and EFTA will be moving closer to each other, while Eastern Europe no longer exists as a separate socio-economic or geopolitical region. While it remains to be seen how far east the integrative process will extend, several trade agreements between Western and Eastern European countries have already been signed, and more comprehensivene ones appear to be in the making. There are bound to be implications for the export opportunities of developing countries, and concern about adverse ramifications is mounting.

A. Economic integration and co-operation in a wider "European Economic Space"

1. The formation of a single EEC market

90. The EEC member States have committed themselves to the formation of a single European market without internal frontiers by the end of 1992, but tough bargaining still lies ahead on a number of issues. A great many private European and foreign companies are preparing for the changes which will be brought about by the creation of a single market. For many of them, broadening and strengthening their European base has become a strategic priority. As regards developing countries, a key issue is whether EEC trade policies will evolve in a liberal or a non-liberal direction. With few exceptions, enterprises in developing countries do not have the financial resources or the global organization of production and distribution to circumvent protectionism in Western Europe by supplying the market of the EEC from local production units. Should protectionism in the EEC increase, exporters of manufactures in developing countries will be the main ones to lose.

2. The strengthening of economic relations between the EEC and the European Free Trade Association (EFTA)

91. EFTA countries[58] are also becoming increasingly apprehensive about the effects of the formation of a single Community market on access for their exports of goods and services to the EEC, as the EEC 1992 Programme may affect the current symmetry in which EEC and EFTA have comparable access to each other's markets. The EEC and EFTA are currently engaged in negotiations for the extension of the existing bilateral free trade arrangements to all essential features of the single European Market. Negotiations between the two groups are to be concluded in time for an agreement on a European Economic Space (EES) to enter into effect by 1 January 1993. Such an arrangement may result in a substantial extension of present preferential EFTA-EEC relations to cover areas such as agricultural trade, government procurement, services, investment, and others. The EES, if realized, will affect third countries inside and outside Europe. With the further removal of barriers to intra-European trade and the encouragement of greater competition, the materialization of the EES could also contribute to a reinforcement of trade among European countries. Moreover, Europe is likely to absorb a substantially larger share of the world's foreign direct investment than in the past.

3. EEC and EFTA: Trade policies vis-à-vis countries in Eastern Europe

92. The EEC and its member States have in the past made extensive use of quantitative import restrictions and anti-dumping measures in their trade with East European countries, relegating them to the bottom of the hierarchy of the EEC's trade policy *vis-à-vis* non-members. Many of the restrictions have been on textiles, footwear, chemical products, some electronic components, toys, glassware and ceramics, some wooden products, the metallurgy sector, including steel, and the agricultural sector.

93. The liberalization of trading arrangements, which began in 1988, was given new impetus by the economic reforms launched in a number of countries in Eastern Europe. Trade and co-operation agreements have been concluded by the EEC with most countries in Eastern Europe, including the Soviet Union.[59] In these agreements, the EEC has committed itself to the progressive removal of quantitative import restrictions by 1995 at the latest, excluding however most of the agricultural sector as well as sectors such as steel and textiles, for which other less liberal sectoral agreements exist, (see para. 62).

94. EFTA countries are also prepared to expand their trade and economic co-operation with the countries in Eastern Europe. Three joint declarations of co-operation were signed in June 1990 with Hungary, Poland and Czechoslovakia, which include provisions for the joint examination of the possibilities of establishing free trade areas with the three countries.[60] Should the EFTA countries conclude free trade agreements with countries in Eastern Europe, possibly along the lines of the EFTA-Spain Free Trade Agreement of 1979, such agreements would need to conform with GATT Article XXIV and hence would have to cover essentially all trade.

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58 Austria, Finland, Iceland, Norway, Sweden, Switzerland.

59 Hungary (1988), Poland, Soviet Union (1989), Czechoslovakia, Bulgaria, Romania (1990). See for a detailed analysis S. Nello, "Some recent developments in EC-East European economic relations", *Journal of World Trade*, vol. 24 (1990).

60 Finland has already concluded free trade agreements with a number of East European countries. See also *EFTA-Information*, 13 June 1990.

B. Systemic changes and need for structural adjustment in countries in Eastern Europe and the USSR

95. Economic reforms continue in Eastern Europe, though their scope and pace differ from one country to the other. Hungary, Poland and Czechoslovakia are moving decisively towards the creation of fully-fledged market economies. In other Eastern European countries and the USSR, the debate concerning concrete reform plans and the speed of their implementation has not yet been concluded.

96. The countries in Eastern Europe and the USSR face daunting economic problems with a substantial slowdown in economic growth and a sharp rise in unemployment in the immediate future. Aggregate industrial output stagnated in 1989 and declined considerably in 1990 (see annex table I.5). Systemic change, a task for which there is no precedent, is being made more difficult by the current external circumstances that these countries are facing, which include the oil shock of 1990 and the switch to convertible currency trading among CMEA countries planned for January 1991. As a consequence, the terms of trade of all countries in Eastern Europe have deteriorated, and are expected to deteriorate even more sharply in 1991. For its part, supply difficulties are not allowing the USSR to take advantage of more favourable international prices for its exports.

97. Faltering economic performance and exports have essentially been the result of inadequate domestic policies in the past, mainly investment policies, as fixed investment has largely been misdirected to less productive areas. The countries in Eastern Europe and the USSR have tended to specialize in products having a low degree of processing and a high intensity in raw materials and energy. Even after the oil price shocks in the 1970s, there was virtually no response in energy consumption in these countries, while energy consumption per unit of output fell sharply in the developed countries.[61] Allocative strategies favoured heavy industry at the expense of consumer goods and technology-intensive investment goods. Excess demand on domestic markets provided little incentive to enterprises to engage in the additional effort to develop export markets. As a consequence, design and marketing skills have long been neglected. The resulting pattern of production is neither in line with world market demand nor in accordance with the comparative advantage of most East European countries.

98. Furthermore, the assured market in the Soviet Union has in the past reduced considerably the necessity for East European countries to modernize obsolete equipment and achieve improvements in production efficiency. Substantial structural changes will result in the patterns of production and trade of the countries in Eastern Europe once their trade with the Soviet Union switches to world pricing and convertible-currency settlement. The East European economies will be forced to reduce their imports of energy and raw materials from the Soviet Union. Heavy industry, notably the metallurgical and chemical sectors, based on the supply of inputs from the Soviet Union, will face adjustment problems on a large scale. At the same time, engineering goods from East European countries can no longer rely on the Soviet Union as their main market outlet as the latter will purchase machinery, equipment and technology to a greater extent from producers in other countries. The cost of structural adjustment will undoubtedly be massive.

C. The implications for export prospects of developing countries[62]

1. The implications of EEC 1992

99. While the once-and-for-all increase in Community income which the formation of a single market is expected to bring about may yield export gains to developing countries, the removal of internal barriers within the Community is, on the other hand, likely to lead to some displacement of their imports by supplies from within the Community. At the aggregate level, increases in im-

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61 See IMF, *World Economic Outlook*, May 1990, Washington, p. 68.

62 For a more detailed analysis, see UNCTAD secretariat, *Trade and Development Report, 1990*, pp. 79-87.

ports from developing countries stemming from higher incomes within the Community may be roughly equivalent to the import replacement effects that result from lower costs of production and greater efficiency within the EEC.

100. The impact, of course, will vary from commodity to commodity. Producers of raw materials of which the Community is a net importer, particularly oil, will benefit from the positive income effects, while import replacement effects will be negligible. In some manufacturing industries, the 1992 Programme is not expected to lead to lower costs of production in the EEC. Thus import replacement may be insignificant in the case of industries which have already achieved a high degree of specialization and market integration within the EEC. This is the case of the textiles and clothing industry. Although the income elasticity of demand for the products of this industry is low, import-increasing income effects may well predominate over import-replacement effects. In other industries where there may be significant unexploited scale economies (e.g., electronics, some types of machinery and chemicals), trade-replacing effects could predominate.

101. On the other hand, some redistribution of gains among the developing economies may occur as a result of changes in EEC trade policy related to the 1992 Programme. Thus, liberalization could affect ACP exporters of certain tropical products, notably bananas, which at present enjoy guaranteed access to the market of the EEC. At least three member States of the EEC limit at present banana imports from non-ACP suppliers through the imposition of quantitative restrictions. The removal of these restrictions could adversely affect ACP suppliers, who may prove to be less competitive than exporters in Latin America.

102. Trading partners of the Community would also suffer setbacks as a result of trade diversion, if the completion of the single market were to be associated with a rise in protectionism. Fears exist in particular that non-tariff barriers in the more restrictive countries of the EEC may be adopted by the EEC as a whole. Pressures to pass on to trading partners the adjustment costs arising from the completion of the Single Market need to be resisted.

2. The implications of the Southward enlargement of the EEC

103. The access of Spain and Portugal to the markets of the other EEC members will improve considerably once the two countries are fully integrated into the Community. At present, they are still in a transitional period, which extends for industrial products up to January 1992 and for agricultural products up to January 1996. The potential effects on developing countries of the full implementation of the southward enlargement of the EEC to comprise Spain and Portugal will depend on the configuration of a number of factors. On the one hand, the markets of the new members could become more open for imports from all or some developing countries on account of the realignment of their tariff structures to the generally lower common external tariff of the Community and the accession of the new members to the association and trade preference agreements that the EEC maintains with several groups of developing countries. On the other hand, eventual free access by Spain and Portugal to the market of the Community will increase competition in this market for a number of export products from developing countries. These include vegetables, citrus fruit, olive oil, fish products and wine from Mediterranean countries; clothing and footwear from Mediterranean, some ACP and South-East Asian countries; steel from some Latin American countries and the Republic of Korea; and other goods such as leather, pulp and paper, wood products, cork and some chemicals and machinery from a variety of developing countries. Furthermore, with the termination of the special trade agreements with countries in Latin America, Spain and Portugal are likely to import various agricultural products such as cereals, livestock and dairy products, which will be brought under the protectionist mechanisms of the EEC's common agricultural policy, increasingly from other EEC member countries rather than from Latin America.

104. As already noted, developing countries are competitive exporters to the Community in a number of product lines in which Spain and Portugal also have significant exports to other EEC countries. The developing countries have generally a competitive advantage on account of lower labour costs, and this advantage may become more pronounced when labour costs in the new member countries rise as a consequence of a greater convergence of wages in an integrated Community market. It is, therefore, important that protectionist pressures that may arise on this ac-

count be resisted.

3. Implications of reforms in Eastern Europe and the USSR

105. The opening up of the economies of Eastern Europe and the USSR to international trade could have several implications for developing countries. One of the results of the changes under way in these countries could be the creation of new export markets for developing countries. Another possibility could be the intensification of competition between producers in Eastern Europe and the USSR and those in developing countries in the markets of the industrialized countries, in particular those of Western Europe.

(a) Potential for new export opportunities in Eastern Europe and the USSR

106. As the economies of Eastern Europe and the USSR become more open to international trade, a greater number of developing countries may gain opportunities to increase their exports to these countries. Increased exports to these markets could meet hitherto unsatisfied demand or, to some extent, replace trade among countries in Eastern Europe and the USSR, reflecting a shift of these economies towards more competitive sources of supply.

107. There is strong pent-up demand in the countries in Eastern Europe and the USSR for food products, other consumer goods and consumer durables, and domestic supply capability for such products remains for the time being insufficient. However, in the short run, foreign exchange shortages and severe external indebtedness will constrain the capacity of countries in Eastern Europe for expanding imports significantly to meet consumer demand. In the Soviet Union, severe supply difficulties will cut into exports in the short term. For the energy importing countries, these balance-of-payments difficulties will be worsened by the impact of the Persian Gulf crisis and the switch to world pricing in trade with the Soviet Union. The need to alleviate critical shortages of food and other basic consumer goods may nevertheless make it necessary for some countries to increase imports of these products, some of which could come from developing countries. Some developing countries are also able to supply modern machinery and technology which meet world market standards, but may have to offer export finance on payments terms as favourable as those granted by developed countries, if they want to compete successfully.

108. Prospects for developing countries in these markets could be more positive in the medium term, if and when foreign exchange constraints ease. The export prospects of developing countries for raw materials (oil, minerals and metals, iron ore, timber products, etc.) could improve in the markets of Eastern Europe as low-priced deliveries on a barter basis from the Soviet Union to other East European economies will come to an end. Moreover, the requirements of reconstruction in the economies in Eastern Europe could boost demand for copper and aluminium. Demand for food imports is also likely to grow. Many developing countries are competitive suppliers of a variety of cereals, cereal substitutes, fruit and vegetables, and animal products and can meet import requirements in Eastern Europe and the Soviet Union. Developing countries exporting consumer manufactures may also have good export prospects in some of these markets.

109. The future course of trade and other economic policies in countries in Eastern Europe and the Soviet Union will strongly influence the export prospects of the developing countries in these markets. Policies in these countries having the effect of increasing gradually but decisively their participation in international trade would be most beneficial to all trading partners, including developing countries. If, on the other hand, in the face of mounting economic difficulties, they were to adopt defensive policies, including protection against imports, the beneficial effects on other countries would be much less. In this case, barriers to market access could turn out to be higher for imports from developing countries than for those from developed countries, particularly those from Western Europe. Closer economic ties with these latter countries would presumably mean that preferential access to Western European markets would have to be reciprocated by Eastern European beneficiaries.

(b) Potential for increased competition in the markets of the developed market-economy countries

110. In the short term, the countries in Eastern Europe and the Soviet Union are unlikely to generate competitive exports in product lines where developing countries have a significant presence (leather and leather products, textiles, furniture, clothing, travel goods, domestic appliances, telecommunications, recording equipment, and electrical machinery) which are sufficiently large to replace exports from developing countries to developed countries on a substantial scale. The East European countries, and in particular the Soviet Union, are barely represented with such goods in the markets of the developed economies (see annex tables II.1 and II.2). Export expansion is limited by insufficient supply capability, outdated technologies, low quality of output, and lack of familiarity with concepts such as marketing and cost control.[63] Moreover, strong pent-up domestic demand and widespread shortages are likely to constrain further the scope for export expansion in some sectors.

111. In manufacturing sectors where production consists essentially of labour-intensive assembly operations which require little capital investment and make use mainly of imported supplies of production inputs, foreign investment could lead to some, although initially still modest, export expansion. The manufacture of clothing and the assembly of television sets and consumer electronics are cases in point. Such exports from developing countries could, to some extent, be unfavourably affected, in particular if foreign investment in Eastern Europe involves a relocation of outward processing and subcontracting from the developing economies to the economies in Eastern Europe.

112. In the medium term, production capabilities can be expected to be built up in keeping with the factor endowment of these countries and with world demand. For developing countries, competition in developed country markets could increase in commodities and in some manufacturing sectors. For example, in the area of primary commodities, the Soviet Union has large resources of non-agricultural raw materials, including oil, iron ore, metals and minerals, and timber products. The country is making efforts to expand its supply capabilities and, in the medium term, may step up its exports of commodities, particularly oil.[64] In the manufacturing sector, countries in Eastern Europe are likely to place emphasis on expanding and diversifying skill-intensive consumer goods industries, on improving the quality of their output, and on the manufacture of more technology-intensive machinery and equipment. The Soviet Union has plans to expand the output of petrochemicals and manufactured forestry products such as fibre board and plywood.[65]

113. Investment by foreign entrepreneurs has apparently not yet gained momentum. Joint ventures and licensing and subcontracting arrangements have been proposed by foreign partners in the following manufacturing sectors: (i) consumer goods (i.e. television manufacture, video-recorders, household appliances, clothing); (ii) motor cars, automotive components, and transport equipment; (iii) industrial machinery; and (iv) chemicals. These investment proposals can be taken to provide some, though incomplete, indication of evolving patterns of industrial supply capabilities in Eastern Europe.

114. Over the medium term, structural changes could consequently emerge which will move at least part of the production of manufactures for export into sectors in which a growing number of developing countries are demonstrating export supply capabilities. The pace of structural change in Eastern Europe will vary among countries, and those which have already a relatively broad and diversified industrial base such as Czechoslovakia, Hungary and Poland will progress at a faster pace. The competition which will arise for developing countries will vary accordingly.

115. Economic policies will play a pivotal role in shaping future trade relations. Governments in developed countries, in particular in Western Europe, are showing a strong political determination to establish closer economic links with countries in Eastern Europe, and several of the latter are likely to be granted easier market access, as is demonstrated by recent liberalization measures. Preferential treatment could increase the potential for trade diversion at the expense of the more

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[63] See A. Inotai, "Competition between the European CMEA and rapidly industrializing countries in the OECD market for manufactured goods", *Empirica-Austrian Economic Papers*, vol. 1 (1988).

[64] See G. Graziani, *Gorbachov's Economic Strategy in the Third World*, (Praeger: Washington, D.C.) 1990, chapter 4.

[65] *East-West*, No. 478, (Brussels, April 1990); and *Outlook for the Forest and Forest Products Sector of the USSR*, United Nations publication, Sales No. E.89.II.E.24.

industrialized developing economies and could place the East European countries so favoured in an advantageous position *vis-à-vis* those developing countries.

Chapter II

STRUCTURAL POLICIES AND TRADE-RELATED ENTERPRISE STRATEGIES IN JAPAN AND IMPLICATIONS FOR EXPORTS FROM DEVELOPING COUNTRIES

116. The limited propensity of the Japanese economy to import manufactures which could be observed up to the mid-1980s has, in no small part, been the reflection of the relative self-sufficiency of the country's industrial structure. Until the early 1970s, industrialization strategies in Japan had aimed to develop nearly the entire gamut of manufacturing industries. Manufacturers could largely procure their production inputs from a well-developed system of domestic sub-contractors with competitive technology and skill levels. The domestic market was large enough to support such a broad-based approach towards industrialization.

117. In spite of relatively low formal barriers to trade, the Japanese market has long been found to be difficult to penetrate by foreign firms. Business practices, domestic laws, and structural characteristics of the Japanese economy (recently highlighted in the trade discussions between the United States and Japan which have come to be known as the "Structural Impediments Initiative") may have contributed to Japan's low propensity to import manufactures. These include government procurement practices favouring Japanese firms; the unique brand of co-operation between Government and business found in Japan; complex licensing, testing and certification requirements found to be onerous by foreign firms; a distribution system which favours family-operated stores, which normally do not stock imports; the "keiretsu" system of business conglomerates, which discriminates against non-group suppliers; and low levels of public consumption - and, consequently, high savings rates.

118. While industrial restructuring commenced already in the late 1970s, it has become a central objective of Japan's economic policy since 1985 when the yen started to soar. Japan's business establishment and the Government stepped up their efforts to transform the structure of Japanese industry, moving it away from its self-sufficient nature towards greater specialization. Current Japanese industrial policy aims at promoting a shift towards higher value added and technologically more advanced fields, with R & D playing a major role. Moreover, the internationalization of production by Japanese firms has speeded up since the early 1980s, and a significant share of such production abroad has been for the production of inputs or components for Japanese firms serving their domestic market. As regards trade policy, several measures have been taken to improve market access for foreign suppliers. The most recent such measures were taken as a result of the Structural Impediments Initiative.

119. The surge in Japanese imports generally, and in imports of manufactures in particular, since 1985 is one result of this interrelated set of factors. The tripling of manufactured imports in value terms since 1985 is a welcome development, and its continuation should make an important contribution to world economic growth. Japan's imports of manufactures from developing countries remain, however, highly concentrated on suppliers in Asia, in particular developing economies on the Pacific Rim (PACRIM) - Hong Kong, Indonesia, Malaysia, Philippines, Republic of Korea, Singapore, Taiwan Province of China, and Thailand.

120. While the share of manufactured imports from Japanese affiliates in Asia in Japan's total imports of manufactures from the region is still relatively low, it has been growing. The importance of Japanese foreign affiliates in Japanese imports varies considerably as between sectors. In

most industries affiliates play a minor role: however, in non-ferrous metals they are significant (about a third of imports), and in four sectors (general machinery, electrical machinery, transportation equipment and precision equipment), their share in Japanese imports is overwhelming. Typically, around three quarters of Japanese imports from Asia in these commodities are shipped by Japanese foreign affiliates. Moreover, in 1986 products from just these four sectors accounted for 74 per cent of all Japanese imports from manufacturing affiliates in Asia, and the electrical machinery and electronics sector alone accounted for 50 per cent.

121. Therefore, the evidence indicates that, in the machinery and precision instruments industries, Japanese foreign direct investment plays a critical role in Japanese imports from Asian developing countries, in particular the PACRIM countries. However, the main factors accounting for the growing importance of these countries in Japanese imports of manufactures appear to be related to their competitiveness *vis-à-vis* other suppliers and their having supply capabilities in those goods which are in high demand in the Japanese market.[66] Other developing countries seeking rapid growth in exports to the Japanese market in sectors other than machinery and instruments will have to place emphasis on policies which promote the development of competitive supply capabilities. On the other hand, developing countries seeking to penetrate the Japanese market for machinery and instruments will probably have to attract investment by Japanese corporations.

Chapter III

STRUCTURAL ADJUSTMENT IN THE UNITED STATES AND EXPORTS FROM DEVELOPING COUNTRIES

122. Its obdurate trade deficit and poor export performance is an indication that the United States is facing a serious structural adjustment problem which must be tackled with long-term policies to strengthen the sector producing tradable goods and services. The trade deficit is, in no small part, the result of a decline in the competitiveness of the productive base of the United States relative to those of its major trading partners. The growth of labour productivity has been sluggish, particularly as compared to other major developed economies. And the growth of business investment has kept significantly below the average of OECD countries.[67]

123. Many companies in the United States appear to have too short-sighted a view as they seemingly concentrate on quarterly changes in their balance sheets rather than on investment strategies that strengthen international competitiveness in the long run. Moreover, excessive corporate take-over activity tends to divert the attention of managerial resources away from tasks which ensure the long-term prosperity of the enterprise. Research and development expenditures, on the other hand, appear to be low and declining, and the educational system needs to be strengthened.

124. Considerable improvements in the competitiveness of the supply side of the United States economy may be required if the trade deficit is to be reduced significantly. Further depreciations of the dollar can achieve this objective only at the expense of relative living standards. The strengthening of the competitiveness of the productive base depends crucially on the initiation of a more vigorous process of structural adjustment by private sector agents in line with changing competitive positions in international trade. A serious threat to such an adjustment process is the increasing resort by the United States (as by practically all major trading countries) to non-tariff barriers, and in particular "voluntary" grey-area measures, to protect weak production sectors against import competition.

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66 Robert Z. Lawrence, "An analysis of Japanese trade with developing countries", *UNCTAD Review* (1991, forthcoming).

67 See: OECD, *Economic Outlook*, various issues.

125. An orderly process of structural adjustment combining greater scope for market processes and judicious government policies to assist in, and reduce the costs of, the needed adjustment would undoubtedly lead to a substantial increase in imports from developing countries in a wide variety of sectors, including agricultural staples such as sugar, clothing, steel, electronic consumer goods, and some types of machinery. At the same time, the trade deficit would decline and income levels would rise, as resources are transferred from low-productivity sectors to those producing for world markets.

Chapter IV

ECONOMIC LIBERALIZATION, EXCHANGE RATE POLICY AND EXPORT SUPPLY CAPABILITY: SOME OBSERVATIONS ON THE EXPERIENCE OF DEVELOPING COUNTRIES

126. Since the early 1980s, a growing number of developing countries have pursued policies aimed at increasing the openness of their economies. This trend has been identified in recent reports by the secretariat. For example, of a sample of 32 countries analysed in *Trade and Development Report 1989*, in the period 1980-1988 only six had not introduced significant import liberalization measures. At the other end of the spectrum, six countries (Bolivia, Côte d'Ivoire, Jamaica, Mexico, Republic of Korea, and Uruguay) had embarked on a major liberalization of their trade regimes. As of end 1988, in the sample of 32 countries there were nine which had low tariffs and few non-tariff restrictions.[68] In 1989-1990 an additional four countries (Argentina, Brazil, Peru and Venezuela) introduced far-reaching liberalization measures. Moreover, the liberalizing trend has spread beyond the countries included in the sample, particularly in Latin America and Africa. Examples of countries introducing wide-ranging trade policy reforms in the period since 1985 include Guatemala, Nicaragua and Paraguay in Latin America and Togo and Guinea in Africa.

127. These policy shifts have been based on the consideration that economic liberalization would help improve the international competitiveness of the productive base and its export supply potential. Many developing countries have embarked on economic liberalization in the context of structural adjustment programmes urged upon them by major international financial institutions. The details of the implementation of such policies - directed both at more liberal trade regimes and domestic deregulation - are complex in practice and remain the topic of widespread debate.

128. One approach has been to implement initially policy measures aimed at increasing exports through the provision of export incentives, the maintenance of a competitive exchange rate for exporters, and allowing exporters access to imported inputs at world market prices, leaving broader import liberalization for a later stage, after export growth has been consolidated. The experience of some major exporting developing countries in South-East Asia since the early 1960s, and of Turkey in the 1980s, with this approach indicates that several policy features have played a crucial role in the successful implementation of this strategy.

129. Firstly, countries did not pursue liberalization precipitately, but took considerable time in passing through the transition period (in the case of the South-East Asian countries, over two decades) from the start of their export drives to the achievement of more open and deregulated economies at the end of the 1980s. And scope for further liberalization still remains now. Secondly, real exchange rates, once depreciated, have been kept at competitive levels.[69] Thirdly, the

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[68] UNCTAD secretariat, *Trade and Development Report, 1989*, pp.121-124.

[69] The importance of the exchange rate factor has been underscored in recent cross country research showing that the rates of growth of output and investment are associated positively with stable real exchange rates; on the other hand, there seems to be only a weak association between import regimes and growth. In many developing countries, an

structure of protection did not discriminate unduly against exports, as roughly equal incentives were provided to exports and domestic sales, though the level of protection differed considerably among production sectors.

130. In the more successful industrializers, the timing and phasing of reductions in protection took account of the degree of competitiveness reached by individual industries. In these cases, the lowering of protection was an additional stimulus to improving efficiency. Furthermore, not too many industries were promoted at once, thereby preventing scarce resources and technical and entrepreneurial talent from being spread too thinly across too many production sectors. Sectoral development strategies were continuously monitored with the objective of assuring that the promoted sectors gradually achieved competitive strength enabling them to face foreign competition and to penetrate export markets. Governments kept a close watch over the export performance of assisted industries and the magnitude of incentives provided, and demonstrated political ability to revise and, if necessary, to terminate interventions if there was no movement towards the desired goal. Close interactions between the Government and the private sector have been an important element in the process of formulation and implementation of sectoral development strategies.[70]

131. Some of the more recent experiences with trade liberalization have involved fairly rapid movement in the direction of liberalizing imports and reducing other government controls. It is difficult to generalize as to the appropriateness of these policies, since several of the countries adopting them were also facing severe internal and external disequilibria which conspired against the success of the trade liberalization programmes. In several of these countries the reforms have been introduced fairly recently, and some are still in their early stages; therefore, it is too early to pass judgment on a number of these experiences. However, given current circumstances, it is difficult to envisage a strong output response from these policy changes. Several of these countries are still suffering from the effects of the debt crisis, and investment is depressed because of the unavailability of foreign exchange. The combined presence of external disequilibria and strong domestic inflation is making the exchange rate difficult to manage. The ensuing instability in the real exchange rate is depressing investment and casting doubts on the sustainability of the trade reforms themselves, which is an additional cause for the failure of investors to respond to the reforms.[71] In some countries, the reduction in tariff levels has tended to aggravate an ongoing fiscal crisis and, therefore, to stoke inflation.

132. The experience of the 1980s seems to show that a staged process is likely to lead to more successful structural adjustment than drastic import liberalization. Those countries which have emphasized export growth first through more realistic exchanges rates and gradual and selective liberalization while paying attention to building up supply capabilities through fiscal and monetary incentives have exhibited relatively fast rates of growth of exports, output and investment. Thus, countries such as Indonesia, Malaysia, Mauritius, Pakistan, Thailand and Turkey, where priority was given to strengthening and diversifying exports and where import liberalization was selective, achieved higher rates of growth of output and superior export performance than countries which relied heavily on broad-based import liberalization to achieve structural change and adjustment (see annex table II.3).

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important reason for the failure of a depreciation to increase export supply has been the inability of the authorities to ensure that the real exchange rate fell significantly and remained at its depreciated level for long enough to permit adjustment of supply. See R. López, "Trade policy, growth and investment", mimeo, Washington, D.C., World Bank, 1989; and O.E.G. Johnson, "Currency depreciation and export expansion", *Finance and Development*, vol.24, No.1, (March 1987).

70 H. Pack and L.E. Westphal, "Industrial strategy and technological change: theory versus reality", *Journal of Development Economics*, vol. 22 (1986); L.E. Westphal, "Industrial policy in an export-propelled economy: Lessons from South Korea's experience", *Journal of Economic Perspectives*, Vol.4, No.3 (Summer 1990); and A.H. Amsden, *Asia's Next Giant: South Korea and Late Industrialization*, (New York and Oxford, Oxford University Press, 1989), chapters III and IV.

71 In a recent paper, Rodrik argues that policy sustainability is an important criterion in the design of successful adjustment measures. As regards trade policy reform, he argues in favour of ensuring strong output responses and reduced price instability before the introduction of thorough-going liberalization measures. See D. Rodrik, "How should structural adjustment programmes be designed?", *World Development*, vol.18, No.7 (July 1990).